

Message Text

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USOECD ALSO FOR EMBASSY

E.O. 11652: NA
TAGS: EGEN, BR
SUBJECT: MISSION'S ECONOMIC TRENDS REPORT - HIGHLIGHTS

1. SUMMARY. IN 1977 BRAZIL MADE SUBSTANTIAL PROGRESS IN IMPROVING ITS EXTERNAL PAYMENTS POSITION AND IN REDUCING INFLATION. THE OUTLOOK IS LESS CLEAR FOR 1978, PARTLY BECAUSE OF DROUGHT IN THE AGRICULTURAL SOUTH-CENTER REGIONS OF THE COUNTRY.

2. SINCE LATE 1976 THE BRAZILIAN GOVERNMENT HAS
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PURSUED A POLICY OF LOWER GROWTH. HAVING RELIED LARGELY ON MONETARY MEASURES, THE AUTHORITIES CONCLUDED THAT THEY WOULD HAVE TO RESTRAIN PUBLIC SECTOR INVESTMENT SPENDING, WHICH HAD BEEN INCREASINGLY RAPIDLY IN THE PRECEDING YEARS. IN A FURTHER STEP, FINANCE MINISTER SIMONSEN, IN MAY 1977, WAS GIVEN NEW POWERS TO CONTROL PRICES. RESULTS OF THESE NEW POLICIES BEGAN TO BE

FELT BY MID-1977. THE 46.3 PERCENT INFLATION RATE OF 1976 WAS REDUCED TO 38.8 PERCENT IN 1977.

3. BRAZIL'S CURRENT ACCOUNT DEFICIT WAS \$3.9 BILLION IN 1977, COMPARED TO \$6.0 BILLION IN 1976. THE TRADE ACCOUNT SHOWED A SMALL SURPLUS OF ABOUT \$140 MILLION. BRAZIL'S EXTERNAL FINANCING REQUIREMENTS WERE SUBSTANTIALLY LOWER IN 1977 THAN IN PREVIOUS YEARS. THE EXTERNAL DEBT, PUBLIC AND PRIVATE, REACHED AN ESTIMATED \$31.2 BILLION; FOREIGN EXCHANGE RESERVES ROSE TO \$7.2 BILLION.

4. BRAZIL'S GDP WAS ON THE ORDER OF \$164 BILLION IN 1977, OR \$1,452 PER CAPITA, IN TERMS OF CURRENT DOLLARS. REAL GDP GROWTH FELL TO 4.7 PERCENT, WELL BELOW THE 9.2 PERCENT GROWTH OF 1976, CONTRIBUTING TO A GROWING SENSE OF FRUSTRATION IN VARIOUS SECTORS OF THE ECONOMY. POWERFUL INDUSTRY ASSOCIATIONS, PARTICULARLY THE CAPITAL GOODS AND ELECTRICAL EQUIPMENT MANUFACTURERS, HAVE EXPRESSED FEAR OF GROWING EXCESS CAPACITY FROM 1978 ONWARD. SOME ASSOCIATIONS ARE DEMANDING FURTHER PROTECTION FROM IMPORTS AND RESTRICTIONS AGAINST THE NEW ENTRY OF FOREIGN FIRMS.

5. IN 1978, EFFORTS TO IMPROVE THE BALANCE OF PAYMENTS AND THE FIGHT AGAINST INFLATION WILL CONTINUE TO GUIDE UNCLASSIFIED

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BRAZILIAN POLICY, BUT THE TASK WILL BE COMPLICATED BY THE EFFECTS OF THE DROUGHT. THE AUTHORITIES HOPE TO HOLD PRICE INCREASES THIS YEAR TO A 30-35 PERCENT RANGE. EXPORTS WILL SUFFER FROM SUPPLY SHORTAGES OF CERTAIN AGRICULTURAL PRODUCTS AND ARE UNLIKELY TO SHOW SIGNIFICANT GAINS. BECAUSE OF THE MIX OF POLICIES CHOSEN BY THE GOVERNMENT, THE ECONOMY'S RATE OF GROWTH MAY BE marginally higher. END SUMMARY.

6. OVERALL PERFORMANCE
BRAZILIAN ECONOMIC POLICYMAKERS STRESSED TWO PRIORITIES IN 1977: A SUBSTANTIAL REDUCTION IN THE INFLATION RATE, PARTLY THROUGH RESTRAINT ON INVESTMENT SPENDING BY PUBLIC SECTOR COMPANIES; AND IMPROVEMENT IN EXTERNAL PAYMENTS, BY EXPANSION OF EXPORTS AND CONTINUED RESTRAINT ON IMPORTS.

7. YEAR-END RESULTS FOR 1977 INDICATE THAT PROGRESS WAS MADE IN BOTH AREAS, PARTICULARLY IN THE TRADE SECTOR. INFLATION, AS MEASURED BY BRAZIL'S GENERAL PRICE INDEX (A WEIGHTED AVERAGE OF DOMESTIC WHOLESALE AND RETAIL PRICES), DECLINED FROM 46.3 PERCENT IN

1976 TO 38.8 PERCENT. THERE WAS SIGNIFICANT IMPROVE-
MENT IN BRAZIL'S TRADE ACCOUNT, WHICH WAS REFLECTED
IN A REDUCED CURRENT ACCOUNT DEFICIT. EXPORTS
INCREASED 20 PERCENT IN 1977 TO \$12.1 BILLION.
IMPORTS DECLINED SLIGHTLY, LEAVING A SMALL TRADE
SURPLUS OF \$140 MILLION, THE FIRST SURPLUS IN FOUR
YEARS. ABOUT HALF OF THE INCREASE IN EXPORTS WAS ATTRIBUTABLE
TO MANUFACTURED AND SEMI-
PROCESSED GOODS, WITH THE OTHER HALF REPRESENTING
HIGHER EXPORT RECEIPTS FROM PRIMARY PRODUCTS, ESPE-
CIALY AGRICULTURE. EXPORTS OF THE CAPITAL GOODS
SECTOR SET THE PACE WITH A 46 PERCENT INCREASE,
SETTLING IN AT \$1.3 BILLION FOR THE YEAR. SOYBEANS
AND SOYBEAN PRODUCTS (INCLUDING OIL) WERE IN SECOND
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PLACE, RISING BY 21 PERCENT TO \$2.1 BILLION. COFFEE
(INCLUDING SOLUBLE) WAS THE LARGEST EXPORT ITEM,
CLOSING AT \$2.6 BILLION. EXPORTS OF IRON ORE DECLINED
TO \$908 MILLION.

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8. THE GOVERNMENT'S ANTI-INFLATION PROGRAM, NOT SURPRISINGLY, RESULTED IN SHARPLY LOWER ECONOMIC GROWTH. GDP, IN REAL TERMS, ROSE BY ONLY 4.7 PERCENT, COMPARED TO 9.2 PERCENT IN 1976. GOVERNMENT-DECREED MONTHLY ADJUSTMENTS TO WAGES, WHICH HAD TENDED TO EXCEED THE COST-OF-LIVING FROM 1974 UNTIL THE THIRD QUARTER OF 1976, HAVE SINCE BEEN HELD BELOW COST-OF-LIVING INCREASES. WHILE IN RECENT MONTHS THE AUTHORITIES HAVE PERMITTED WAGE ADJUSTMENTS TO EXCEED THE ANNUAL RATE OF INCREASE IN THE GENERAL PRICE INDEX, WAGE INCREASES HAVE NEVERTHELESS CONTINUED TO LAG BEHIND
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INFLATION AS MEASURED BY INCREASES IN THE COST-OF-LIVING.

9. LOOKING TO 1978, GOVERNMENT OFFICIALS HAVE SPOKEN OF CONSOLIDATION OF THE RESULTS ACHIEVED IN 1977. THE BASIC OBJECTIVES ARE:

- (1) MAINTENANCE AND, IF POSSIBLE, ENLARGEMENT OF THE TRADE SURPLUS;
- (2) FURTHER REDUCTION IN INFLATION; AND
- (3) CONTINUATION OF MODERATE ECONOMIC GROWTH (I.E., 5-6 PERCENT REAL GDP INCREASE).

POLICIES TO PURSUE THESE OBJECTIVES INCLUDE LOW CEILINGS ON BANK CREDIT, CLOSE CONTROL OVER WAGES AND PRICES, AND MAINTENANCE OF THE EXPORT INCENTIVE SYSTEM FOR MANUFACTURED GOODS. SEVERE IMPORT RESTRICTIONS ARE ALSO EXPECTED TO CONTINUE. THE AUTHORITIES ARE PERMITTING MODEST GROWTH IN PUBLIC SECTOR INVESTMENT SPENDING (UP ABOUT 10 PERCENT IN REAL TERMS) AND HAVE APPROVED SOME INCREASE IN LENDING BY THE NATIONAL DEVELOPMENT BANK (BNDE). THESE MEASURES ARE EXPECTED TO PROVIDE A MILD STIMULUS TO THE INDUSTRIAL SECTOR.

10. THE GOVERNMENT'S EFFORT WILL BE COMPLICATED BY THE EXPECTED DECLINE IN AGRICULTURAL PRODUCTION--LARGELY DUE TO DROUGHT IN THE SOUTH-CENTER REGIONS--AND BY LOWER WORLD MARKET PRICES FOR CERTAIN AGRICULTURAL COMMODITIES, ESPECIALLY COFFEE. THIS COMBINATION OF FACTORS IS LIKELY TO CUT INTO AGRICULTURAL EXPORTS, SUCH AS THE IMPORTANT SOYBEAN AND COFFEE GROUPS. IN ADDITION, THE AUTHORITIES WILL

HAVE TO RESORT TO IMPORTS TO MEET SUPPLY SHORTAGES IN THE DOMESTIC MARKET AND CURTAIL UPWARD PRESSURES ON PRICES.

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11. INFLATION AND MONETARY POLICY
WHOLESALE PRICES ROSE MORE SLOWLY IN 1977 THAN THE GENERAL PRICE INDEX--35.5 PERCENT AS COMPARED WITH 38.8 PERCENT--AND SIGNIFICANTLY LESS THAN THE 44.9 PERCENT RISE IN WHOLESALE PRICES IN 1976. ON THE OTHER HAND, THE COST OF LIVING IN RIO DE JANEIRO CONTINUED TO INCREASE MORE RAPIDLY THAN THE GENERAL INDEX; AT 43.1 PERCENT, THE RATE SHOWED LITTLE CHANGE FROM 1976 (44.8 PERCENT). IN A NUMBER OF OTHER CITIES, COST-OF-LIVING INCREASES SIGNIFICANTLY EXCEEDED THE RIO INDEX.

12. FACTORS REDUCING PRESSURE ON PRICES WERE THE POLICIES HOLDING FINANCIAL (E.G., MONETARY CORRECTION) AND WAGE ADJUSTMENTS BELOW THE PREVAILING RATE OF INFLATION. USING A MOVING WEIGHTED AVERAGE OF THE WHOLESALE PRICE INDEX FOR THE PRECEDING 12-MONTH PERIOD (BEGINNING IN JULY 1975), AVERAGE WAGE ADJUSTMENTS DURING THE MONTHS JULY 1976 TO DECEMBER 1977 AMOUNTED TO APPROXIMATELY 91 PERCENT OF INCREASES IN THE INDEX; MONETARY CORRECTION ADJUSTMENTS AMOUNTED TO ONLY ABOUT 79 PERCENT. IN ADDITION, THE MINISTER OF FINANCE USED HIS NEW POWERS OVER ADMINISTERED PRICES TO SLOW INCREASES, THUS SEEKING TO REVERSE INFLATIONARY EXPECTATIONS.

1. THE GOB WAS SUCCESSFUL IN LOWERING INFLATION DESPITE AT BEST ONLY MODEST MONETARY RESTRAINT. EXPANSION OF BANK CREDIT TO THE PRIVATE SECTOR ROSE 50.6 PERCENT IN 1977. THE GROWTH OF THE MONEY SUPPLY (M1) WAS 37.5 PERCENT--ABOUT THE SAME AS IN 1976 (37.2 PERCENT). THE HEAVY COST OF AGRICULTURAL CREDIT PROGRAMS AND THE REDEMPTION OF TREASURY BILLS BY PUBLICLY-OWNED CORPORATIONS (ANTICIPATING YEAR-END CASH REQUIREMENTS), WERE PRINCIPAL FACTORS RESPONSIBLE FOR THE EXPANSION OF THE MONEY SUPPLY IN EXCESS OF THE 25 PERCENT GROWTH TARGET. (THE LATTER FACTOR, UNCLASSIFIED

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HOWEVER, WAS PARTIALLY OFFSET BY MEASURES TAKEN BEFORE THE END OF THE YEAR.)

14. IN LATE 1977 THE FINANCE MINISTER MOVED FORCE-
FULLY TO CURTAIL THE RAPID EXPANSION OF THE MONETARY
BASE; MEASURES INCLUDED (1) A FIRM CEILING ON BANK
OF BRAZIL CREDIT, (2) INCREASES IN RESERVE REQUIRE-
MENTS FOR PRIVATE COMMERCIAL BANKS TO 40 PERCENT
(CASH AND TREASURY BILLS), (3) AN INCREASE IN THE
REDISCOUNT RATE TO 30 PERCENT, AND (4) TEMPORARY
STERILIZATION OF THE PROCEEDS OF EXTERNAL LOANS AT
THE END OF 1977 (NOW LIFTED).

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15. THE GOVERNMENT'S MONETARY BUDGET FOR 1978 ANTI-
CIPATES SHARP REDUCTIONS IN BOTH CREDIT AND MONEY
SUPPLY GROWTH RATES. OVERALL CREDIT TO THE PRIVATE
SECTOR IS SLATED TO EXPND 31.9 PERCENT DURING 1978,
WITH LENDING FOR AGRICULTURE EXPANDING BY 32.4 PERCENT.
THE MONEY SUPPLY INCREASE IS PROVISIONALLY TARGETED

AT 25 PERCENT.

16. INDUSTRY

INDUSTRY WAS HIT HARD BY THE GOVERNMENT'S ANTI-INFLATION POLICIES. THE SECTOR GREW AT ABOUT 4 PERCENT
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IN 1977, AS AGAINST 11 PERCENT IN 1976; MANUFACTURING WAS DOWN FROM 10.2 PERCENT TO 2.3 PERCENT. THE AUTOMOBILE INDUSTRY SHOWED AN ABSOLUTE DECLINE; AUTOMOBILE PRODUCTION WAS 912,000 UNITS, DOWN FROM 985,000 UNITS IN 1976. THE ELECTRICAL-ELECTRONIC INDUSTRY GREW BY 5 PERCENT, COMPARED WITH 35 AND 20 PERCENT IN 1975 AND 1976. BOTH INDUSTRIES ARE HEAVILY CONCENTRATED IN THE SAO PAULO AREA.

17. LEADING INDUSTRIAL GROWTH IN 1977 WAS IN STEEL, CAPITAL GOODS, PETROCHEMICALS, AND CEMENT. STEEL PRODUCTION ROSE BY 21.5 PERCENT, REACHING 11.2 MILLION TONS. OUTPUT OF MECHANICAL CAPITAL GOODS (INCLUDING MACHINE TOOLS, TEXTILE MACHINERY, AND HEAVY MECHANICAL EQUIPMENT) INCREASED BY 10.2, CEMENT BY 12.0, ASPHALT BY 14 PERCENT (THROUGH NOVEMBER). ON THE OTHER HAND, FINANCING OF HOME CONSTRUCTION BY THE NATIONAL HOUSING BANK (BNH) FELL OFF SIGNIFICANTLY, AND ISSUANCE OF BUILDING PERMITS DECLINED FROM 1976 LEVELS. OVERALL, HOWEVER, CONSTRUCTION ACTIVITY HELD UP WELL, INCREASING BY 9 PERCENT. THE MINERALS SECTOR, ON THE OTHER HAND, REGISTERED A 4.7 PERCENT ABSOLUTE DECLINE, MAINLY RELATED TO WEAK WORLD DEMAND FOR IRON ORE.

18. IN SPITE OF THE LOWER RATE OF GROWTH, THERE IS YET NO EVIDENCE OF A SUBSTANTIAL INCREASE IN UNEMPLOYMENT. HOWEVER, URBAN EMPLOYMENT, ESTIMATED AT 3 PERCENT, IS INCREASING MUCH LESS THAN URBAN POPULATION (6 PERCENT PER ANNUM). IN FACT, THE COUNTRY'S INDUSTRIAL HUB, SAO PAULO, REGISTERED ONLY NEGLIGIBLE GROWTH IN EMPLOYMENT DURING 1977. SOCIAL PRESSURES AND COMPETITION FOR JOBS THUS MAY INCREASE DURING 1978.
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19. EVEN THOUGH THE GOVERNMENT WISHES TO RESTRICT GROWTH TO REDUCE INFLATION AND IMPORTS, MAJOR PROJECTS IN PRIORITY SECTORS, SUCH AS IMPORT SUB-

STITUTION AND HYDROELECTRIC POWER, ARE PROGRESSING RAPIDLY. WORK HAS STARTED ON PHASE III OF THE STEEL EXPANSION PROGRAM; EQUIPMENT ORDERS SHOULD BE PLACED BY THE END OF THE YEAR. CONSTRUCTION OF THE CRACKING UNIT AT THE THIRD PETROCHEMICAL COMPLEX, LOCATED IN RIO GRANDE DO SUL, HAS ALSO BEGUN.

20. ENERGY

BRAZIL HAS SO FAR BEEN UNABLE TO REDUCE ITS HEAVY DEPENDENCE ON IMPORTED OIL, DESPITE AN IMPRESSIVE, VIGOROUSLY ENFORCED OIL CONSERVATION PROGRAM AND THE RAPID EXPANSION OF HYDROELECTRIC POWER. BRAZILIAN CRUDE OIL PRODUCTION IN 1977 TOTALLED 60.8 MILLION BARRELS, 3.4 PERCENT LESS THAN OUTPUT IN 1976 AND JUST 17.3 PERCENT OF THE COUNTRY'S OVERALL PETROLEUM REQUIREMENTS, ACCORDING TO PRELIMINARY DATA. DECREASING PRODUCTION ONSHORE IN THE BAHIA BASIN ACCOUNTED FOR THE DECLINE, MORE THAN OFFSETTING THE INCREASE IN OFFSHORE PRODUCTION. APPARENT CONSUMPTION OF ALL PETROLEUM DERIVATIVES AMOUNTED TO 351.3 MILLION BARRELS, SOME 2.4 PERCENT HIGHER THAN IN 1976. CONSUMPTION OF DIESEL OIL ROSE BY 6.7 PERCENT, WHILE GASOLINE CONSUMPTION DROPPED BY 3.8 PERCENT. PETROLEUM DERIVATIVES ACCOUNTED FOR AN ESTIMATED 40-45 PERCENT OF BRAZIL'S TOTAL ENERGY CONSUMPTION. DURING THE YEAR, EXPLORATION AND DEVELOPMENT ACTIVITIES WERE CENTERED ON OFFSHORE FIELDS. DELAYS WERE ENCOUNTERED IN THE INSTALLATION OF THE PRODUCTION SYSTEM IN THE OFFSHORE CAMPOS BASIN, WHICH IS NOW SCHEDULED TO PRODUCE A TOTAL OF 45,000 BARRELS PER DAY BY 1979. ALCOHOL PRODUCTION

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(TO BE MIXED WITH GASOLINE IN A 1:4 RATION) FROM SUGAR FOR THE 1977-78 CROP YEAR IS EXPECTED TO REACH 1.6 MILLION LITERS (OR 36.8 THOUSAND BARRELS PER DAY), A 150 PERCENT INCREASE OVER THE PREVIOUS YEAR. EXPLORATORY DRILLING HAS NOW BEGUN UNDER THE FIRST OF THE RISK CONTRACTS SIGNED BETWEEN PETROBRAS AND INTERNATIONAL OIL COMPANIES.

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21. IN 1976, BRAZIL'S HYDROELECTRIC POWER PLANTS
FURNISHED A TOTAL OF 81,468 GWH OF ELECTRICITY, ABOUT
ONE-QUARTER OF THE COUNTRY'S TOTAL ENERGY AND A 14
PERCENT INCREASE IN ELECTRIC POWER CONSUMPTION OVER
1975. FOR 1977 CONSUMPTION OF THE RIO-SAO PAULO
AREA IN 1977 WAS UP BY A FURTHER 9.9 PERCENT, REACHING 35.534 GWH.
CONSTRUCTION IS ON SCHEDULE FOR THE \$7
BILLION ITAIPU HYDROELECTRIC PROJECT, WHICH WILL
PRODUCE 12,600 MEGAWATTS OF ELECTRICITY BY 1983;
CONTRACT AWARDS FOR THE EQUIPMENT WILL BE MADE
THIS YEAR. THE GOVERNMENT HAS ALSO INITIATED
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PLANNING FOR THE GASIFICATION OF SOME OF THE COUNTRY'S
LARGE RESERVES OF LOW-QUALITY COAL, WITH TWO PROEJCTS
IN RIO GRANDE DO SUL AND SANTA CATARINA UNDER CON-
SIDERATION; CHEMICAL COMPLEXES WOULD BE LOCATED
ADJACENT TO THE GASIFICATION PLANTS.

22. IN THE NUCLEAR ENERGY FIELD, CONSTRUCTION IS CONTINUING
ON BRAZIL'S FIRST COMMERCIAL NUCLEAR PLANT, ANGRA I, A

WESTINGHOUSE-SUPPLIED 625 MEGAWATT LIGHT WATER REACTOR SCHEDULED TO START OPERATION IN 1979. INITIAL CONSTRUCTION WORK HAS ALSO BEGUN ON TWO GERMAN-SUPPLIED LIGHT WATER REACTORS--THE FIRST TWO UNDER THE GERMAN-BRAZILIAN AGREEMENT--DESIGNED TO SUPPLY AN ADDITIONAL 2600 MEGAWATTS OF ELECTRIC POWER BY THE MID-1980'S.

23. AGRICULTURE

WHILE 1977 WAS A BANNER YEAR FOR BRAZILIAN AGRICULTURE, 1978 IS EXPECTED TO BE A DISAPPOINTING ONE. THE PROLONGED DRY SPELL IN THE IMPORTANT CENTER-SOUTH AGRICULTURAL REGIONS HAS SEVERELY AFFECTED PROSPECTS FOR SUCH IMPORTANT EXPORT COMMODITIES AS SOYBEANS, CORN, AND RICE. SOYBEAN PRODUCTION, WHICH LAST YEAR WAS 12.0 MILLION TONS, WILL BE DOWN SUBSTANTIALLY. IN REGARD TO CORN, OF WHICH BRAZIL EXPORTED 1.4 MILLION TONS IN 1977, IT NOW APPEARS THAT SUBSTANTIAL IMPORTS, UPWARDS OF 1 MILLION TONS, WILL BE REQUIRED TO MEET DOMESTIC NEEDS; IN ADDITION TO WEATHER-RELATED LOSSES, ACREAGE FOR CORN WAS ALSO DOWN BECAUSE OF THE LOW PRICES AT PLANTING TIME LAST NOVEMBER. FOR RICE, A STAPLE ITEM IN THE BRAZILIAN DIET, LARGE GOVERNMENT STOCKS APPEAR TO OBTAIN THE NEED FOR IMPORTS. IT IS STILL TOO EARLY TO ESTIMATE POSSIBLE EFFECTS OF THE DROUGHT ON COFFEE PRODUCTION; REDUCTION FROM EARLIER ESTIMATES, WHICH WERE ON THE ORDER OF 20 MILLION BAGS, ARE LIKELY. NEVERTHELESS, IT APPEARS THAT BRAZILIAN SUPPLIES (INCLUDING EXISTING UNCLASSIFIED

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STOCKS) WILL BE SUFFICIENT TO COVER DOMESTIC AND EXPORT DEMAND.

24. IN VIEW OF THE SMALLER SUPPLIES AND LOWER WORLD PRICES FOR CERTAIN COMMODITIES, NOTABLY COFFEE, AGRICULTURAL EXPORTS ARE LIKELY TO DECLINE. AT THE SAME TIME, OUTLAYS FOR AGRICULTURAL IMPORTS WILL BE HIGHER. WHEAT IMPORTS WILL RISE FROM 2.7 MILLION TONS TO AN ESTIMATED 4.3 MILLION TONS, AT A COST OF APPROXIMATELY \$530 MILLION. IN ADDITION TO CORN, BRAZIL HAS ALSO AUTHORIZED THE IMPORTATION OF UP TO 50,000 TONS OF MEAT. THE GOVERNMENT HAS REMOVED BARRIERS TO THE IMPORTATION OF SOYBEANS FOR PROCESSING AND RE-EXPORT; AT THIS TIME, IT IS UNKNOWN WHETHER THIS WILL OCCUR.

25. FOREIGN TRADE AND PAYMENTS

BRAZIL'S EXTERNAL PAYMENTS POSITION IMPROVED SUBSTANTIALLY IN 1977, BUT FURTHER IMPROVEMENT WILL BE DIFFICULT TO ACHIEVE THIS YEAR. BRAZIL RECORDED A \$2.3 BILLION IMPROVEMENT IN ITS TRADE ACCOUNT FOR 1977, BASED ON A 20 PERCENT INCREASE IN EXPORT EARNINGS TO \$12.1 BILLION, AND A 2.8 PERCENT DECLINE IN IMPORTS TO 12.0 BILLION. THE TRADE SURPLUS OF \$140 MILLION PERMITTED A REDUCTION IN FOREIGN BORROWING COMPARED TO 1976 AND AN INCREASE IN RESERVES TO \$7.2 BILLION AT YEAR END. BRAZIL'S MEDIUM AND LONG-TERM EXTERNAL DEBT, PUBLIC AND

PRIVATE, ROSE TO ABOUT \$31.2 BILLION.

26. COFFEE RECEIPTS INCREASED BY 10 PERCENT, FROM \$2.4 BILLION IN 1976 TO \$2.6 BILLION IN 1977. EXPORTS OF THE SOYBEAN GROUP (INCLUDING OIL) ROSE TO \$2.1 BILLION, COMPARED WITH \$1.8 BILLION IN 1976. COCOA (INCLUDING COCOA BUTTER), SUGAR (NEW AND REFINED), AND ORANGE JUICE ALSO INCREASED IMPRESSIVELY TO \$531 MILLION, \$463 MILLION, AND \$117 MILLION. PRIMARY PRODUCT EXPORTS IN GENERAL EXPANDED BY 14.5 PERCENT, WHILE INDUSTRIAL GOODS EXPORTS GREW 30.2 PERCENT. EXPORTS OF MANUFACTURED GOODS REACHED \$3.5 BILLION, SOME 29 PERCENT OF BRAZIL'S TOTAL EXPORTS IN 1977; CAPITAL GOODS WERE THE STAR PERFORMERS WITHIN THE GROUP, RISING BY 46 PERCENT TO \$1.25
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BILLION. IRON ORE PERFORMED POORLY, WITH EXPORTS FALLING 9.5 PERCENT TO \$908 MILLION.

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27. IMPORTS CONTINUED TO BE SUBJECT TO SEVERE RESTRICTIONS, INCLUDING OUTRIGHT PROHIBITION OF MANY GOODS, A 100 PERCENT PRIOR IMPORT DEPOSIT, THE "LAW OF SIMILARS" (REQUIRING GOVERNMENT ENTITIES TO "BUY BRAZILIAN"), AND HIGH TARIFFS. THE COST OF PETROLEUM IMPORTS INCREASED IN 1977 BY ALMOST 6 PERCENT, TO \$3.0 BILLION, AND ACCOUNTED FOR 32 PERCENT OF BRAZIL'S TOTAL IMPORT BILL. NON-PETROLEUM IMPORTS DECLINED FROM \$8.6 BILLION IN 1976 TO \$8.1 BILLION. INTERMEDIATE GOODS IMPORTS ROSE SLIGHTLY, TO \$3.9 BILLION, PRINCIPALLY FERTILIZERS AND NON-FERROUS METALS, WHILE CHEMICALS DECLINED. CAPITAL GOODS IMPORTS, ON THE OTHER HAND, WERE SUBSTANTIALLY LOWER, AT UNCLASSIFIED

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\$3.1 BILLION AS COMPARED WITH \$3.5 BILLION IN 1976. WHEAT IMPORTS WERE ALSO LOWER, AT \$280 MILLION.

28. WHILE THE AUTHORITIES HOPE TO MAINTAIN AND ENLARGE THE TRADE SURPLUS, THE OUTLOOK FOR 1978 IS NECESSARILY UNCERTAIN. EXPORTS OF MANUFACTURED GOODS SHOULD CONTINUE TO GROW IN 1978, WITH PROJECTIONS RANGING FROM 15 TO 25 PERCENT. ALSO, THE AUTHORITIES SHOULD BE ABLE TO MAINTAIN IMPORTS AT APPROXIMATELY CURRENT LEVELS, EVEN THOUGH SOME ADDITIONAL PURCHASES WILL BE REQUIRED IN THE AGRICULTURAL SECTOR. ON THE OTHER HAND, REDUCED SUPPLIES AND LOWER PRICES WILL ADVERSELY AFFECT AGRICULTURAL EXPORTS. THUS, DESPITE THE GOVERNMENT'S VIGOROUS EFFORTS, IT IS NOT CLEAR WHETHER BRAZIL WILL BE ABLE TO MAINTAIN A TRADE SURPLUS IN 1978.

29. DEPRECIATION OF THE CRUZEIRO AGAINST THE DOLLAR AMOUNTED TO APPROXIMATELY 30 PERCENT IN 1977, AS THE GOVERNMENT MAINTAINED ITS POLICY OF DISCREET SMALL DEVALUATIONS. THE CONTINUED SATISFACTORY GROWTH OF MANUFACTURED-GOODS EXPORTS SUGGESTS THAT THE EXCHANGE RATE DEPRECIATION IN 1977 HAS BEEN ADEQUATE, WITHIN BRAZIL'S EXISTING REGIME OF EXPORT INCENTIVES AND SEVERE IMPORT RESTRAINTS. BRAZIL HAS ENCOUNTERED NO DIFFICULTY IN ARRANGING FOREIGN LOANS IN 1977 AND EARLY 1978, INCLUDING EURODOLLAR BONDS ISSUES. BRAZIL'S BORROWING NEEDS ARE LOWER THAN IN RECENT YEARS AND FUNDS CONTINUE TO BE READILY AVAILABLE IN THE EURODOLLAR MARKET. THE REDUCTION IN THE RATE OF INFLATION AND THE IMPROVING TRADE ACCOUNT HAS CONTRIBUTED TO CONFIDENCE IN BRAZIL AMONG FOREIGN BANKERS. WHILE EXPORT GROWTH APPROXIMATELY EQUALLED THE GROWTH IN FOREIGN DEBT IN 1977 FOR THE FIRST TIME IN SEVERAL YEARS, EXPORT EXPECTATIONS SUGGEST THIS ACCOMPLISHMENT MAY NOT BE REPEATABLE IN 1978.

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30. COMMENT: THIS REPORT IS A JOINT MISSION EFFORT OF
EMBASSY BRASILIA AND THE CONSULATES GENERAL RIO AND SAO PAULO.
FULL TEXT OF THE ECONOMIC TRENDS REPORT, TOGETHER WITH
STATISTICAL MATERIAL, WILL BE SUBMITTED BY AIRGRAM. MISSION
WILL PROVIDE, BY SEPTTEL, CLASSIFIED ASSESSMENT OF THE BRAZILIAN
ECONOMY.
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